COMMUNIQUÉ

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RISK MANAGEMENT - CONTRACTS OF ENGAGEMENT

Managing Professional Risk is one of the most important challenges for the profession in New Zealand today. Any increase in potential liabilities arising from professional practice is a threat to the viability of the profession.

It is an inevitable part of carrying out any professional service that risks are taken. However, these risks can be significantly managed and controlled by Members if they are fully addressed in the Brief and in the Agreement for Architectural Services.

NZIA Agreements for Services

The ***NZIA Agreements for Services AAS2 2000*** & ***Short Form SF1 2000*** have been designed with a purpose to restrict the Architect's liability to those risks the parties intended at the time of the Client's briefing. The intention is to clearly to define the scope of the services in line with the Client's Brief.

Written contracts are the good news. Oral contracts are the ***very bad*** news.

Duty of Care

By accepting any commission a Member contracts to perform the task with the care and skill usually exercised by those in the profession with similar qualifications. This is the test that common law requires an Architect to meet. It is established in common law that a professional standard of practice is maintained. No matter what an Agreement for Services may contain a Member is liable for his or her negligent acts. Such liability is governed by civil law *(i.e. Liability in Tort)*. Liability in Tort is distinctly different from something that simply arises when a contractual provision is breached.

Client Developed Contracts

Legal advisers, project managers or contractors when acting for a Client are increasingly presenting Members with *"non-standard"* conditions of contract. The intention of such is often to transfer some of the Client's risks and liabilities to the Member. In some extreme instances contracts are adapted from construction or maintenance contracts. These forms of contracts for services will inevitably contain many liabilities that lie far beyond the normal responsibilities and duty of care. Such proposed agreements cannot normally be amended satisfactorily without considerable legal input and cost.

When an approach is made in this form for a Member to accept additional risk *(i.e. greater risk than would be required by law)* the question that arises is *"Whose risk would it otherwise be?"* Inevitably, it is likely to be a part of the Client's risk in undertaking the project but the Client is attempting to transfer such risk to the Member.

Non-assumption of Liability

In forming any Agreement for Services, Members should avoid any provision that requires an assumption of liability *(i.e. to do more than the Law of Tort requires).* For example, a provision in an agreement for services that requires performance *"at the highest professional level*" would obligate an Architect to a standard far in excess of that established at common law. If that standard is not met then the contract is breached, thus allowing the Client to formulate a claim for damages in circumstances whereby the Member may not otherwise have been liable.

Promising to perform at a higher-than-ordinary level of care is but one of many examples. Other promises would include any guarantee or warranty of performance or transfer of statutory liabilities such as the Member agreeing to ensure the other parties comply with various statutes, permits and consents.

Extension of Liability

Client prepared agreements for services often include adjectives such as *"all", highest"* and *"best"* and other wording that is intended to increase liability and/or remove certain defences that are available under common law. Also commonplace are words that are often included such as *"indemnity", "hold harmless", "warrants*", *"ensure*", *"comply with", "guarantee"* and others that may mean effectively the Member will be required ***to pay*** when things go wrong ***without*** the benefit of any insurance funding.

At common law it is necessary for a plaintiff, including any Client, when suing a Member to prove the following:

- The Member failed to adhere to the standard of care one would expect of a normal competent practitioner carrying out the engagement.
- Breach of that standard caused the plaintiff to suffer the loss.
- The loss suffered by the plaintiff was reasonably foreseeable by the professional at the time the breach occurred
- The amount of the loss suffered.

If a plaintiff can prove these four elements then the Member may be able to reduce the amount of liability by proving one or more of the following.

(1) The plaintiff voluntarily assumed the risk of the loss.

(2) The plaintiff has been guilty of contributory negligence and having regard to this responsibility, the loss should be reduced to such an extent as is just and equitable.

(3) The plaintiff has failed to act reasonably to mitigate the loss.

In broad terms these doctrines in common law have a degree of flexibility to them so as to enable the Court to adjust the position between the parties to the extent that it is believed to be just and equitable.

If a Member accepts a liability beyond the common law duties as described above or in fact compromises his or her legal defences then there may be no insurance cover to necessarily respond.

Limitation of Liability

Client prepared conditions of engagement often do not include any ***time or monetary*** limitations. An important issue that can be overlooked by members is that a contractual requirement to insure, is just that, and does ***not*** limit the Member's liability in any way to the amount of the available insurance.

Indemnifications

Members should be extremely wary of any *"indemnity"* or *"hold harmless"* provisions in an Agreement for Services that can have the effect of making a Member liable to make good a Client's loss regardless of the Member's degree of culpability. Such a responsibility may apply even though the Member's performance has measured up to the accepted standard and the Member has not been negligent. An *"indemnity"* or *"hold harmless"* agreement can mean a contractual responsibility to pay monies to a Client or other parties, regardless of fault.

There are both procedural and substantive implications in respect of any claim under an indemnification clause The substantive implications depend upon the wording of the indemnity but often an indemnity may refer to loss or damage *"arising out of or in consequence or carrying out the service"* or similar. Indemnities may also contain words that on the face of it are not limited to loss or damage to the extent caused by the negligence of the Member. Also it may make reference to the inclusion of "*solicitor/client legal costs"* that would mean, in effect, the Member would be paying for the Client's legal costs to sue.

The procedural implications are also of significance. Claims against Members under the NZIA Agreements for Services almost invariably involve ordinary civil proceedings, with the plaintiffs understanding they will have to ultimately fully establish the elements of their claim at a trial. An indemnity could expose Members to the possibility of summary judgments, at least on liability but in many cases also on quantum. This could have very serious connotations for the conduct of any defence.

Insurability Problems

Members should recognise that *"assumption of liability"* can create significant insurability problems, because professional indemnity policies only provide coverage for breach of professional duty that arises from negligent acts or omissions and certain other civil claims.

If a Member assumes a liability under contract and then merely fails to deliver on that promise this is unlikely to be covered by insurance.

The overall liability lesson is quite clear, continue to support and use the ***NZIA Model Agreements for Services*** otherwise insurability will become a serious issue that cannot reasonably be dealt with without considerable legal input and advice.

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We welcome contributions from readers, on how they manage risk.